

VZCZCXRO5798
RR RUEHCN RUEHGH
DE RUEHGZ #8103/01 1720837
ZNR UUUUU ZZH
R 210837Z JUN 06
FM AMCONSUL GUANGZHOU
TO RUEHC/SECSTATE WASHDC 1444
INFO RUEHOO/CHINA POSTS COLLECTIVE
RUCPDO/USDOC WASHDC
RUEAIIA/CIA WASHDC
RUEKJCS/DIA WASHDC
RHHMUNA/HQ USPACOM HONOLULU HI

UNCLAS SECTION 01 OF 02 GUANGZHOU 018103

SIPDIS

SIPDIS

E.O. 12958: N/A

TAGS: [ECON](#) [EFIN](#) [EINV](#) [KPAO](#) [CH](#)

SUBJECT: PAS Speaker Barth Relates U.S. Banking Experience to China

¶1. SUMMARY: Visiting speaker James Barth spoke to banking regulators, attorneys, and students in Guangzhou about the development of financial systems and similarities between the U.S. and China experience. He highlighted the role of governments in banking industry bailouts, foreign ownership of banks, and the futility of imposing a universal model for financial regulation. Attendees appreciated Barth's enthusiastic presentations and participated eagerly in the discussions. END SUMMARY

¶2. James Barth is a participant in the China Mission's visiting speakers program. He is currently the Lowder Eminent Scholar in Finance at Auburn University and a Senior Fellow at the Milken Institute. He recently served as leader of an international team advising the People's Bank of China on banking reform and coauthored a book titled "Rethinking Bank Regulation and Supervision: Till Angels Govern". During his June 13-14 visit to Guangzhou, Barth held separate meetings with officials from the China Banking and Regulatory Commission, attorneys from H.J.M. law office, and students and professors from Sun Yatsen and South China Normal universities.

Similarities with the U.S. Experience

¶3. In his presentations, Barth drew parallels between the development of financial systems in the United States and China. For example, during the first 60 years of the United States, U.S. banks were owned by state governments, with politicians sitting on boards and ordering loans to particular companies or industries. Separately, U.S. banks in the 1980's earned approximately 90 percent of their income from interest rates, similar to China's banks today. Since then, U.S. banks have developed a number of services, the fees of which account for half of their total income. Lastly, the U.S. banking industry was faced with massive non-performing loans in the late 1980's, in part because of overinvestment in the real estate sector. To avert a widespread crisis, the U.S. government spent USD 200 billion to bail out its banks -- reflecting China's current efforts to recapitalize its own banks.

China Has Room to Improve

¶4. Barth also contrasted the characteristics of the U.S. and Chinese financial systems. China's system is oriented toward banking (with the big four state-owned banks accounting for over half of the industry's assets). The U.S. system, however, is capital market intensive, with stock and bond markets serving as key sources of funding for companies. Chinese companies thus are without a "spare

tire" -- in the event of a banking collapse, companies cannot easily generate money from alternate sources. Barth also noted the lack of deposit insurance in the Chinese system. Deposit insurance, which guarantees that investors will recap their money in the event of a banking crisis, is a vital part of any healthy banking system. Fortunately China is reportedly drafting just such a law. Barth also said that China needs to increase the amount of banks loans to small and medium enterprises. He discussed his successful efforts to convince U.S. banks that a low-rate credit card for SMEs is profitable.

Who Should Control the Banks?

15. During discussions, participants revealed a particular interest on the role of the private sector and foreign ownership in China's banking industry. Barth estimated that 98 percent of China's banking industry is controlled by the government, in comparison to none in the United States and United Kingdom. He said foreign investment undeniably brings benefits to the banking industries of developing countries, including managerial skills, technology, and funding. Nevertheless, there is no definitively "correct" amount of foreign investment for all countries. Both the United States and New Zealand have healthy banking industries, despite the fact that foreign ownership in the U.S. banking industry is 20 percent while in New Zealand it is 98 percent. In China's case, Barth said the government is pursuing a logical course by targeting foreign ownership in particular regions and in smaller banks before opening up its big four banks.

A Universal Model Does Not Exist

GUANGZHOU 00018103 002 OF 002

16. Students and regulators reacted positively to Barth's enthusiastic presentation style as well as the substance of his talks. They asked questions about the effect of the Sarbanes-Oxley Act on U.S. competitiveness, China's real estate boom, and the ideal model for regulation of a financial industry. In response to the latter question, Barth said no such model exists and those who proclaim a universal solution are misguided. Each country is unique, particularly in the development stage of their government and commercial institutions, and thus each requires a different model. Indeed, a country may have "beautiful" financial laws, which exactly reflect those used by the most developed countries, but still suffer from slow growth and weak capital markets.

Comment

17. It is noteworthy that so many students were interested in what is ordinarily considered a dry subject. This may be in part because the Chinese press has made China's financial industry an everyday topic. Regardless, educated Chinese people realize that their country's financial institutions are in fact important to their lives and seem genuinely interested in learning from the U.S. experience.

DONG